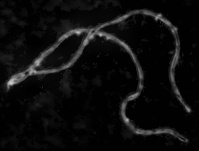

Supreme Court [illegible]

[illegible]

LOUISVILLE TRUST COMPANY, [illegible]

vs.

STUART R. KNOTT [illegible]

BRIEF FOR APPELLEES.

ALEXANDER P. HUMPHREY,
[illegible]

[illegible]

28439

Supreme Court of the United States.

OCTOBER TERM, 1903.

LOUISVILLE TRUST COMPANY, RECEIVER, . *Appellant*,

vs.

STUART R. KNOTT ET AL., *Appellee*.

This is an appeal prosecuted from the judgment of the Circuit Court of the United States for the Western District of Kentucky, dismissing the application of the appellant to have the properties and assets of the Evening Post Company, then in the custody of the Court's Receiver, Mr. Lewis C. Humphrey, turned over to the appellant, an appointee of the Jefferson Circuit Court.

FACTS.

We think it would conduce to a clear understanding of the questions if we should make a statement of facts out of which the controversy arose.

The Evening Post Company was a corporation created under the general incorporation law of Kentucky, having a charter which expired on the 1st day of May, 1903. A few days before this date it developed that forty-eight out of a total issue of six hundred shares of stock in this Company were held by the estate of Walter N. Haldeman. The executors of Haldeman's estate only a few days before the expiration of the charter produced that stock and had it transferred to their names. The Haldemans are the owners and controllers of the Courier-Journal and the Louisville Times, competitive papers of the Evening Post. When the Haldeman ownership became known it became evident that there could not be an amicable reorganization of the Evening Post Company. Thereupon a meeting of stockholders was called, and at that meeting every share of stock was represented. All of the stock except that held by the Haldemans was voted to appoint the Columbia Finance and Trust Company agent as liquidator, to wind up the affairs

of the corporation. The forty-eight shares controlled by the hostile interests objected to every move made, but the resolution appointing the Trust Company as liquidator was adopted, and the liquidator accepted the trust. The hostile stockholders also demanded the right to inspect the books, papers, accounts and all the private transactions of the Evening Post Company, which a competing interest would like to be advised of. This was denied, but the liquidator was directed to make up and furnish to each stockholder a comprehensive statement of the assets and liabilities of the corporation.

After the appointment of the liquidator, the hostile stockholders, through their attorney, made a demand upon the liquidator for a statement of the assets, and were assured that such a statement would be forthcoming. They then made a demand for a statement of the liabilities, specifying in detail how they wanted the statement made, and they were assured this statement would be made, and it was made. (Rec. 37.) They then repeated their demand for the right of personal inspection of the books, papers and affairs of the Evening Post Company. This was refused, and they then brought suit in the State Court in the nature of a suit for a mandatory injunction to compel the officers of the Evening Post Company to permit the Haldeman interests to personally inspect the affairs of the Post Company. That suit was brought on the 12th day of May, 1903. The petition appears on pages 25 to 30, inclusive. Answers were filed. A motion was made on May 19th for an order permitting the plaintiffs to have the inspection desired, and the case was proceeding in the State Court solely to accomplish that object. In the intervening petition, the appellants treat the hearing of that motion as the hearing of of the cause, as in fact it was. (R. 18.) The language of the petition is that "the hearing of said cause was begun" etc., "on May 23, 1903." Reference to record, page 31, will show that the motion for an inspection was the only matter before the Court on the 23d of May, 1903. The hostile interests had taken the position that the Post ought to stop publication, because it was losing money, and when they brought their suit they asked in their prayer that the Court determine whether or not the affairs of the Evening Post Company should be continued in operation, and if so, that the operation of the plant be conducted under and subject to the orders of the Court. (R. 30.)

At this point it became evident that a determined attack was to be made upon the continuation of the publication of the paper. If the publication should be suspended, certain valuable assets, like the Associated Press franchise, and others, would be imperiled and the value of the assets of the Evening Post

Company, no longer a going concern, would be depreciated from 50 to 75 per cent. When this became apparent, Stuart R. Knott, one of the creditors, brought a suit in the Circuit Court of the United States for the Western District of Kentucky, and obtained a judgment, and thereafter, execution having issued and being returned *nulla bona*, this suit in equity was brought by him for himself and all other creditors, for the purpose of taking charge of the assets of the Evening Post Company, and winding them up in such a way as would bring the greatest price. To that end steps were taken to continue the publication of the paper so that it might be sold as a going concern. The Receiver of the Federal Court was appointed on the *28th day of May*, 1903, and qualified and took charge of the property immediately. On the *4th day of June*, 1903, nearly a week afterwards, the State Court granted the application of the Haldemans for an inspection of the books and papers and affairs of the Evening Post. They then applied to the proper officers of the Evening Post Company and to the liquidator, the Columbia Finance and Trust Company, armed with this order of the State Court, and demanded this inspection, but of course at that time the only answer to be given was that the property was in the charge of the Federal Court, and that the officers and liquidator had no control over the books and were unable, therefore, to permit the inspection. *On the 27th day of June*, 1903, a month after the appointment by the Federal Court, the State Court appointed the appellant Receiver of the Evening Post Company, and in the same order referred the case to its Commissioner to advertise for creditors. The Federal Court also appointed a Commissioner with the usual instructions to advertise for creditors and audit and report their claims. None of the creditors appeared in the *State Court*, or proved or offered to prove their claims in that case, *but all of them appeared* in the Federal Court, and proved their claims before the Federal Court Commissioner, and we represent these creditors as well as the complainant. The report of the Commissioner of the Federal Court appears on pages 61 to 63 inclusive. It appears from that report that creditors holding claims amounting to $119,163.51 presented their claims before the Commissioner of the Federal Court. This report was filed on *July* 6, 1903. (R. 13.) The intervening petition was filed the same day. (R. 13.)

On these facts, the question now arises whether the Circuit Court of the United States for the Western District of Kentucky erred in refusing to surrender control over assets acquired almost a month before the State Court was asked or undertook to appoint a receiver, *or to take any steps looking to the administration of the estate of the Evening Post Company.*

We submit that the Court did not err for the following reasons:

1st. The plaintiffs in the State Court had no right to bring a suit for the settlement of the estate of the Evening Post Company. The plaintiffs in that suit are mere stockholders. It does not add to the legal argument to point out that they only held 8 per cent. of the entire stock, and that it is obvious the stock was not really worth the paper it was written on, except in so far as it may affect the question to be later discussed as to what was the real object of the suit. For the purposes of this point now under discussion we treat them simply as stockholders. The general incorporation law of Kentucky, section 561, provides that "when any corporation expires by the terms of the articles of incorporation, or by the voluntary act of its stockholders it may thereafter continue to act for the purposes of closing up its business, but for no other purpose, and it shall be the duty of the officers to settle up its affairs and business as speedily as possible; and they shall cause notice to be published for at least one week for four consecutive weeks in some newspaper printed and published in the county, if any, of the fact that it is closing up its business; and all debts and demands against the corporation shall be paid in full before the officers receive anything."

Every stockholder of a corporation organized under the general law is bound by that provision of the statute which enters into and becomes a part of the compact between the stockholders, and no stockholder has a right to set aside or ignore the inexpensive method of winding up the corporation and to substitute in lieu of it, the cumbersome and expensive suit in Chancery, unless he can show some equitable ground justifying the appeal to Chancery. In this case no attempt has been made to do that. No allegation of fraud is made, no complaint is made that the liquidator would act in an oppressive way toward the stockholders. No facts are alleged whatever that would justify a court of equity in disregarding this plain provision of the statute intended to be binding upon all stockholders. The only averment made on that subject in the petition in the State Court is found on pages 29 and 30, and is as follows:

"Plaintiffs state that it is impracticable and impossible to have a fair, just and proper accounting and settlement of the business and affairs of the said Evening Post Company except herein, and that in view of the persistent conduct of the defendants, hereinabove set out, they will not and can not be advised or informed of the assets and liabilities of the said Company until the defendants are compelled to furnish such information

herein, and are compelled to allow the plaintiffs to inspect and examine the books, accounts and affairs of the said Evening Post Company."

The persistent conduct referred to there is the refusal by the officers of the Evening Post Company to allow the Haldemans, representing hostile interests, free access to investigate all of the intimate affairs of the Evening Post Company. That allegation certainly does not amount to a sufficient reason for a court of equity undertaking the settlement of the whole estate of the Evening Post Company in order that the Haldemans might know the extent of the assets and liabilities. Furthermore, the answer of the defendants shows that before that suit was brought, statements of the assets and liabilities made out precisely according to the request of the Haldemans had been sent to and received by them. This statement was made out by an expert accountant selected by the liquidator, which is a leading reputable trust company, and there is no pretense for saying that the Haldemans were not advised of the extent of the liabilities and assets. That is the only reason given for going into a court of equity, and we submit that it is no reason whatever, and that the Haldemans have failed to show any sufficient reason for not being bound by the statute.

It is, however, contended by them that the statute was not followed in this case, in that the officers had not proceeded to wind up the estate as provided by the statute. We think there is little merit in this contention. The stockholders holding the great majority of the stock and the real owners of the paper, desiring to continue the publication of the paper, expected to become bidders at the sale of the property. This they could not do if they were also the sellers. Therefore, in order not to be embarrassed, legally or otherwise, by this situation, the whole body of stockholders acting by the majority, which included everybody except the small interest of the Haldemans, appointed the Columbia Finance and Trust Company, a highly reputable concern, the liquidator, in order that the business might in all respects be fairly and impartially transacted, so that any stockholder might protect his interests by becoming a bidder. We think this was a proper course for the stockholders to pursue, and it was no justification for the small dissenting interests held by the Haldemans to go into a court of equity and to attempt to have a cumbersome and expensive settlement. The liquidator had the right, so far as the stockholders were concerned, to proceed to advertise for creditors and to advertise the estate for sale, and to sell it and distribute the proceeds.

2d. It was not the real object of the suit to have a settlement. Upon this point we invite the Court's attention to the

petition in the State Court. (R. 25 to 30 inclusive.) The Court will perceive that there is not a single averment even tending to show that the parties had come into Court for a settlement of the whole estate, except that which we have quoted, and except the prayer itself, but the prayer does not help out the failure to make the proper averments, and the pleader does not seem to have had in his mind the necessity for stating such facts as might justify a stockholder in repudiating the method of settlement provided by statute and seeking a settlement in equity. No case is stated for a receiver, and none is prayed for.

3d. Even if the obvious purpose of the plaintiffs in the State Court had been to have a settlement, that does not necessarily imply that the Court would take possession of the property itself. The Court need not take possession merely to settle disputed questions for the guidance of the liquidator, but could leave to it the duties imposed upon it by the stockholders of advertising for creditors and advertising the property for sale, and selling and distributing the proceeds under the orders of the court. The prayer of the petition does not expressly or by implication involve the idea of the Court itself taking possession of the property.

4th. This suit, however, does involve that idea, and the creditors had the right to institute this suit and take possession of the property, and have it properly conserved by the orders of the Court, as has been done, and have it sold as a going concern and the proceeds distributed in the Federal Court itself. That was the object of the suit and the Receiver of the Court took charge of the property and had had charge of the property for a month, before the State Court was asked to or did take any action whatsoever looking either to a settlement of the estate or to the taking possession of the property.

5th. The parties to these two cases are entirely different. In the State Court case stockholders are plaintiffs and no one is made a defendant except the stockholders. The suit is, therefore, essentially one involving a quarrel between those who would be owners of the property after the payment of its debts.

In the proceeding in the Federal Court, however, the complainant is a creditor, suing on behalf of himself and all others similarly situated. The defendants are the old corporation, the liquidator and the officers of the old corporation. The bill of complaint explains exactly why all these persons are made defendants.

If the corporation had continued in existence after the expiration of its charter, then no one need have been made parties to the creditor's bill except the corporation, or except

the corporation and the liquidator, assuming that this liquidator stood in the place of a trustee. But if the proper construction of the Kentucky statutes in reference to dissolved corporations is that upon the expiration of the charter the property of the corporation vests in its then officers as trustees, these officers are proper parties.

So that the creditors might in every event be secure in their remedy against the property of this insolvent corporation, the bill of complaint makes all persons parties who would be proper parties in any view of the case. The petition in the State Court did not make any one a defendant who was not also a stockholder. It is true that the petition filed in the State Court alleged that the defendants were the only persons known to the plaintiff who claimed to be creditors. (R. 29.) But the answer of the Columbia Finance and Trust Company, filed in the State Court (R. 36-37), shows that prior to the filing of the petition in the State Court the Columbia Finance and Trust Company had furnished the plaintiffs a list of the creditors.

The allegation is specifically made, and called for a reply from the plaintiffs. This may be found on page 49 of the Record, and is in this language:

"They deny that the liquidator, Columbia Finance and Trust Company, or any other person, ever prepared or furnished any information to the plaintiffs touching the matters set forth in their petition, until after the preparation and completion thereof as filed."

From this careful statement it is apparent that prior to the time that the plaintiffs filed their petition in the State Court they had a full list of the creditors furnished to them, and that their only denial of this is that the list was not furnished until after their petition had been prepared.

The plaintiffs, then having before them a list of the creditors of the Evening Post, entirely failed to bring before the Court any one of them except such as were stockholders. And that they were challenging these debts is apparent from the petition.

Again, in the printed brief for appellant, at page 37, there is quoted from the Kentucky Code of Practice the following section:

"432. A creditor appearing before the Commissioner and presenting his claim becomes thereby a party to the action and is concluded by the final judgment of the Court allowing or rejecting his claim."

The fact is, however, that in the State Court case the plaintiffs gave no opportunity to the creditors to come before the Commissioner until long after a Receiver had been appointed in the Federal Court. In other words, it was not until a month after the Receiver was appointed in the Federal Court that the case in the State Court was referred to the Commissioner; and it must be obvious that, until the case was referred to the Commissioner, a creditor would have no opportunity to go before him with his claim.

The case in the Federal Court, however, was, from its very inception, a creditors' suit. The bill is filed on behalf of Stuart R. Knott and all other creditors. The prayer is for the marshaling of the assets and for the appointment of a receiver, and abundant reasons were given for the appointment of a receiver to take into custody the assets of this insolvent corporation. So that in the Federal Court case the complainant at once moved the Court to appoint a receiver, as he had prayed in his bill. And the creditors promptly came forward and proved their claims in the Federal Court, and had so proved them prior to the time that any effort was made by the Louisville Trust Company, Receiver of the State Court, to intervene in the Federal Court.

If it is true that a suit between stockholders will prevent the creditors of an insolvent corporation from filing a creditors' bill to subject the property of the corporation to their demands, then it must be likewise true that if one partner files a bill against his co-partners, asking a settlement of the partnership estate, this will prevent the seizure of any of the partnership property by process of law on the part of any of the creditors of the partnership.

The position, therefore, that the appellant must sustain in this case is of the most radical character and involves the doctrine that a stockholder of a dissolved corporation, or a partner of a dissolved partnership, can bring a suit against his co-stockholders or his co-partners, in a court of equity, and ask the Court to administer the insolvent estate. He need not pray for a receiver, nor ask that one be appointed. To the contrary, he may leave the assets in the possession of the corporation or of a liquidator, or of the co-partners, and this proceeding will, in and of itself, deprive all other courts of jurisdiction over these assets; and these assets—all of them—being in the constructive possession of the Court, can not be attached, nor levied upon at the suit of a creditor, nor taken possession of by a receiver at the suit of a creditor. The simple filing of such a bill is sufficient to impound the assets, constructively or portentially, and put an end to the jurisdiction of all other courts, so far as such assets are concerned. And this, too, in a case where no cred-

itors except co-stockholders or co-partners are made parties, and no reference made to a commissioner to bring in any such creditors.

We hardly think it necessary to undertake a review of the authorities upon this question in view of the able opinion of the lower Court, which does it so well. We, however, call the Court's attention to the case of Shields vs. Coleman, 157 U. S. 177, as settling one proposition which in our opinion is conclusive of this case. In that case the Federal Court had appointed a receiver, and then, having accepted a bond from the defendant, discharged the receiver and restored the property to the corporation. Thereafter the State Court appointed a receiver and took charge of the property, and then after that, the Federal Circuit Court undertook to again appoint a Receiver and wrest the property from the State Court. This Court held that could not be done. In discussing that question, the Court said:

"For the purposes of this case it is unnecessary to decide whether, as between courts of concurrent jurisdiction, when proceedings are commenced in the one court with the view of the appointment of a receiver, they may be continued to the completion of actual possession, and whether, while those proceedings are pending in a due and orderly way, the other court can, in a suit subsequently commenced, by reason of its speedier modes of procedure, seize the property, and thus prevent the court in which the proceedings were first commenced from asserting its right to the possession. Gaylor v. Fort Wayne, etc. Railroad, 6 Bissell, 286-291, cited in Moran v. Sturgis, 154 U. S. 256-270; High on Receivers, 3d Ed., Sec. 50. Of course, the question can fairly arise only in a case in which process has been served, and in which the express object of the bill, or at least one express object, is the appointment of a receiver, and where possession by such officer is necessary for the full accomplishment of the other purposes named therein. The mere fact that, in the progress of an attachment or other like action, an exigency may arise, which calls for the appointment of a receiver, does not make the jurisdiction of the court, in that respect, relate back to the commencement of the action."

We take the liberty of repeating the test laid down by the Court, which, we think, is conclusive of this case.

"*Of course, the question can fairly arise only in a case in which process has been served, and in which the express object of the bill, or at least one express object, is the appointment of a receiver, and where possession by such officer is necessary for the full accomplishment of the other purposes named therein.*"

Now in the State Court case it is neither the express nor the implied object, nor one of the objects, of the bill to have a receiver, nor was the possession by the Court of the property necessary for the accomplishment of the purposes named in the bill.

While that is unquestionably true as to the State Court, as we have heretofore shown, it is not true as to the Federal Court, and the latter Court, having taken possession of the property at the instance of the creditors for the purposes of settlement, we submit, correctly refused to surrender the property to the State Court.

In Compton v. Jesup, 68 Fed. Rep., 263, it appeared that one Compton had filed a suit in the State Court to foreclose his lien upon certain railroad property. Subsequently, in a bill filed in the Federal Court, receivers were appointed for this same property. The question came up as to the effect of the assumption of jurisdiction by the Federal Court, of this property, under these circumstances. Judge Taft, in delivering the opinion of the Court, said:

"It is further objected that the Court below had no power to take possession of the railroad property by its receivers in 1884, pending the suit of Compton in the Common Pleas Court, to subject the property to the payment of his liens. The argument is that Compton's suit was in the nature of a proceeding *in rem*, which impounded the property, and excluded any other court from assuming actual possession of it. Heidritter v. Oil Cloth Company, 112 U. S. 294; 5 Sup. Ct. 135; is cited in support of this proposition. That was an ejectment suit. The plaintiff claimed under a sheriff's deed executed to a purchaser at a judicial sale by order of a State Court, in a proceeding to enforce a mechanic's lien against the premises in controversy. The defendant claimed under a marshal's deed executed to the purchaser at a judicial sale by order of a Federal Court, in a proceeding under the internal revenue laws, to forfeit the premises because used for illegal distilling. When claims for the mechanic's liens were filed, and suits were brought to enforce the same, in accordance with the New Jersey statute, the premises were in the actual custody of the United States marshal, who had taken possession under process of attachment issued on an information to enforce a forfeiture, which resulted subsequently in a sale, and the deed under which defendant claimed. The sale under the proceedings in the State Court took place a few days after that by the United States marshal. It was held that proceedings begun in the State Court in the nature of proceedings *in rem* to subject the premises to sale were ineffectual to confer any legal title on a purchaser, if at the time they were begun the property was in the actual custody of the Federal

Court for the purpose of a judicial sale by the latter Court. It was not decided, however, that the proceedings in the State Court might not be valid to establish the lien. The holding was expressly limited to the point that a deed under the State proceeding vested no legal title as against the title conferred by the Court first having actual custody of the property. It was the actual custody of the premises in the Federal Court which excluded the right of another court to entertain jurisdiction of a proceeding to subject the property thus removed from its control and disposition to a sale for the purpose of vesting a title superior to that which might be conferred by the Federal Court. Mere constructive possession would not have been enough to exclude possession by another court. In a conflict of jurisdictions it is manifest that there can be no constructive possession by one court, where it can not take actual possession, but it by no means follows that the constructive possession of one court will exclude the actual taking possession by another. For this reason, even if the proceeding in the Lucas Common Pleas to establish Compton's lien was a proceeding *in rem*, it did not involve the actual seizure of the property pending the suit, and did not, therefore, prevent the Federal Court from taking actual possession of the property, through its receivers, in a proceeding to foreclose mortgages and other liens than Compton's. This objection to the jurisdiction of the Court below over the Knox and Jesup bill cannot, therefore, be sustained."

The intervening petition of the appellant contains certain allegations in reference to the reason why the complainant, Stuart R. Knott, brought his suit, and commented upon the fact that judgment was confessed and appearance entered to the suit at law and the bill in equity. And these allegations are brought forward with considerable emphasis in the brief of the appellant, on file. (P. 14-15.)

When the intervening petition was presented, the complainant, Stuart R. Knott, filed exceptions to these allegations on the ground that they were irrelevant and impertinent, and asked that they be stricken out. (R. 14.) As the Court denied the relief asked for in the prayer of the intervening petition, it did not pass upon the motions to strike out.

As is said in Dickerman vs. Northern Trust Company, 176 U. S. 188, "it should be borne in mind, in connection with the several defenses set up by the intervenors, that they do not appear here in the capacity of creditors, but as stockholders; that their rights are the rights of the corporation and must be asserted and enforced through the corporation, and upon the theory that the latter has, or threatens by collusion or otherwise to neglect the proper defense of the foreclosure suit."

We refer to this case as stating very fully the doctrine that the imputation of a bad motive will not be a defense to the assertion of a legal right.

It is not alleged in the intervening petition of the Louisville Trust Company that the Evening Post Company did not owe Stuart R. Knott the amount he claimed. If the debt was a just one, why should not then the Evening Post Company enter its appearance and consent to a hearing of the cause?

Again, the intervening petition does not deny the allegation of Stuart R. Knott's bill of complaint that, if such relief as is therein claimed be not afforded, then the property of the said Evening Post Company will be dissipated or damaged to such an extent that creditors will not obtain anything like what is justly due to them; that there is no remedy at law for the complainant and other persons similarly situated that is in any degree adequate. (R. 5.)

How can it be said that the only purpose of the complainant's bill is to defeat the jurisdiction of the State Court, when the effect of the prosecution of the complainant's bill will be to have a decree of sale of all the assets of the Evening Post and a distribution of the proceeds of such sale among its creditors?

Suppose it to be true that Mr. Richard W. Knott, seeing that if the quarrel went on in the State Court, among the stockholders, the creditors would lose what was justly due to them, did ask his brother, Mr. Stuart R. Knott, to do what he could to prevent this catastrophe? The fact is that the complainant, Stuart R. Knott, brought a suit in the Federal Court, being represented by counsel who had never been employed by nor appeared for any one in the State Court. It is a further fact that judgment was obtained upon the debt of the complainant, execution issued and a return of *nulla bona* made. The intervening petition does not allege that the *nulla bona* return was a false return. It does not allege that there were assets upon which the marshal could have levied to make the debt of Stuart R. Knott. The complainant, Stuart R. Knott, thereupon filed his bill for himself and all other creditors and had a receiver appointed. Suppose that Mr. Richard W. Knott and the other defendants believed that the debt of the complainant was a just one, and that there were many other just debts, and that in order to pay these debts it was necessary to have a receiver appointed, an arrangement made for the continuation of the paper and the proper proceedings taken for the sale of the paper as a going concern—the intervening petition does not deny the truth of any of these things.

It can not be the law that the jurisdiction of the Federal Court depends upon the purpose which a litigant has in view when invoking it. It is sufficient that the litigant has a claim

which is a just claim, and which, under the law, he has a right to assert in that tribunal. And it is a sufficient reason for such litigant's filing a bill in equity to appoint a receiver, that he has such grounds as are sufficient for the appointment of a receiver. These grounds the intervening petition does not dispute.

We respectfully submit that these allegations are mere make-weights; that they are irrelevant and impertinent, and even if every one of them were true, they would present no reason for discharging the Federal Court Receiver and turning over the property to the State Court Receiver. For what, in the meantime, is to become of the rights of the other creditors who have made themselves parties to the Federal Court proceeding, by proving their claims before the Commissioner?

It is not alleged that anybody induced them to prove their claims, or to come forward, as they so promptly did, to take advantage of the bill filed by the judgment creditor.

We respectfully submit, therefore, that there was nothing in this intervening petition which would have justified the Federal Court in giving up the jurisdiction lawfully invoked by the creditors of the Evening Post Company, and in the orderly exercise of which alone the debts of that Company will receive the first consideration and the disputes of the stockholders be relegated to a time when it shall be determined that there is anything left to dispute over.

ALEXANDER P. HUMPHREY,
JAMES P. HELM,
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